

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
PEOPLES TELEPHONE COMPANY, INC.	:	DETERMINATION
	:	DTA NO. 816253
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax Law	:	
for the Periods March 1, 1993 through November 30, 1993	:	
and March 1, 1994 through November 30, 1994.	:	

Petitioner, Peoples Telephone Company, Inc., 2300 NW 89th Place, Miami, Florida 33172, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the periods March 1, 1993 through November 30, 1993 and March 1, 1994 through November 30, 1994.

A hearing was held before Frank W. Barrie, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on September 23, 1998 at 10:00 A.M., with all briefs to be submitted by February 13, 1999, which date began the six-month period for the issuance of this determination. Petitioner appeared by Keith J. Roland, Esq. The Division of Taxation appeared by Terrence M. Boyle, Esq. (Robert J. Tompkins, Esq., of counsel).

ISSUE

Whether petitioner's purchases of pay phone pedestals and enclosures were exempt from sales tax under Tax Law § 1115(a)(12), which provides an exemption from tax for telephone

station apparatus for use directly and predominantly in receiving at destination or initiating telephone communication.

FINDINGS OF FACT

1. Since December 1992, petitioner, Peoples Telephone Co., Inc., has owned and operated pay telephones (“pay phones”) in New York State. Most of petitioner’s pay phones located in New York were acquired through bulk purchases from four companies, which had previously owned and operated the pay phones in New York, as follows: (1) U.S. Telecommunications, Inc. in March 1993, (2) ASCOM Communications, Inc. in November 1993, (3) Telecorp Public Communications, Inc. in April 1994, and (4) Telecoin Communications, Ltd. in October 1994.

2. Peoples Telephone Co., Inc. enters into agreements with property owners, including retailers, to install pay phones. Petitioner owns the installed pay phones and is responsible for their maintenance and the collection of coins. By the end of the period at issue, it had taxable sales from its operation of pay phones in New York, when annualized, of approximately \$10,000,000.00.

3. The Division of Taxation (“Division”) by its auditor examined petitioner’s acquisition of its New York pay phones by reviewing petitioner’s bulk sales contracts with the four companies noted above. The auditor determined that petitioner had \$1,052,768.00 in purchases subject to use tax.¹ Petitioner agreed that its bulk sale purchases of office furniture were subject to tax, but disagreed with the imposition of tax on purchases of telephone pedestals and

¹The tax at issue has been referred to as use tax by the auditor although it is more precisely viewed as sales tax. The use tax, as noted by the Court of Appeals in *Bloomington Bros. v. Chu* (70 NY2d 218, 519 NYS2d 347, 349):

“[W]hich complements the sales tax, taxes uses which have not been and will not be the subject of sales tax [citation omitted]. Because the goods at issue were used in New York, but not sold in this State, it would be the use tax, not the sales tax that would govern.”

In the matter at hand, the goods at issue were the subject of bulk sale purchases by petitioner in New York so that it is technically correct to refer to the tax at issue as sales tax, not use tax.

enclosures of approximately \$860,000.00, which the parties agreed was a reasonable estimate of the portion of the total cost under the bulk sales contracts allocable to pay phone pedestals and enclosures.

4. The auditor determined that sales and use tax of \$70,997.12 was due on petitioner's acquisition of pay phone pedestals and enclosures totaling approximately \$860,000.00, which resulted in the Division's issuing a Statement of Proposed Audit Adjustment dated August 13, 1996 against petitioner asserting tax due of \$70,997.12, plus interest, as follows:

Periods Ended	Tax Due	Interest Due	Total
May 31, 1993	\$ 7,995.41	\$ 2,372.63	\$10,368.04
November 30, 1993	56,173.59	14,157.56	70,331.15
May 31, 1994	6,500.18	1,359.12	7,859.30
November 30, 1994	327.94	52.26	380.20
Totals	\$70,997.12	\$17,941.57	\$88,938.69

5. The Division then issued a Notice of Determination dated September 3, 1996, mirroring the Statement of Proposed Audit Adjustment dated August 13, 1996, which asserted sales and use tax due of \$70,997.12 plus interest against petitioner.

6. The parties have agreed that at issue is whether sales and use tax is due on petitioner's purchase of pedestals and enclosures totaling approximately \$860,000.00. However, the record is inexact concerning the specific pedestals and enclosures purchased by petitioner in the course of the bulk purchases at issue. As noted in Finding of Fact "2", the amount of purchases of enclosures and pedestals of approximately \$860,000.00, which the parties have agreed is at issue, was only a reasonable *estimate*. The narrative section of the auditor's report noted as follows:

The value that was associated with the [pay] telephones [purchased by petitioner in the bulk sales] also included the cost of the booths,² wiring, poles, signs and other items. This amount was not broken down and there was not adequate information to determine this amount. However, in the interest of being fair and reasonable current values of phones and additional items were used to arrive at estimated percentages that were agreeable with both the taxpayer and the auditor. The agreed upon percentage that was allocated to the telephones³ and parts was 91.5%. This left 8.5% that related to the booths, wiring, etc. The telephones are considered exempt station apparatus that is used directly and predominantly to initiate and/or receive telephone communication. The tax due on the booths, wiring, etc. is \$70,997.12.

7. The auditor testified that she received a schedule from petitioner which in her words:

[G]ave the description of the type of enclosures and pedestals that were used and the number of phones associated with that type of [enclosures and pedestals], and the number of phones acquired during the acquisition to tie the type of [enclosures and pedestals] to the number of phones that were used when we were arriving at the percentage to use for the total amount of taxable items from the bulk sale (tr., p. 26).

This schedule, which was labeled “Cost of Peripheral Equipment Acquired- 1993 and 1994 Acquisitions,” shows a total “cost of peripheral equipment acquired” of only \$629,540.00 not \$860,000.00, the amount agreed to by the parties as noted above. Furthermore, the technical descriptions on the schedule of the 16 types of enclosures and pedestals apparently at issue were not all explained. The schedule shows \$478,303.00 as the greatest “cost of peripheral equipment acquired” for one particular type of enclosure and pedestal (out of 16 listed) which was associated with 5,295 phones at acquisition (out of a total number of phones at acquisition of 6,464). This most common “equipment type” was noted as “IEDX 33,” and the description of this particular enclosure and pedestal was as follows, “SALP + Enclosure only, 110V light, Solid/ Sardine.” Petitioner’s witness, Michael Ogrodnick, described this particular item as

² It appears the auditor used the term “booths” to refer to enclosures and pedestals.

³By exempting the “telephone,” the auditor treated “the housing, the coin retriever, anything that was actually part of the physical phone [as exempt]” (tr., p. 35).

“an enclosure only, with a 110 volt light in a solid sardine that goes around a sardine enclosure.

This is a standard pedestal and enclosure that goes on a pay phone” (tr., pp. 47-48).

While later in the hearing, petitioner introduced into evidence technical specifications for five types of pay phone pedestals and enclosures from Independent Enclosures, a manufacturer of pay phone pedestals and enclosures, none of these specifications can be specifically related to this most common type of pedestal and enclosure noted on the schedule or any of the others listed.

Petitioner's Evidence

8. Petitioner presented the testimony of Michael Ogrodnick, its district manager for the region that includes New York City, Long Island, and parts of Westchester and New Jersey. Prior to his employment by petitioner, Mr. Ogrodnick was employed in a similar capacity by ASCOM Communications, Inc., from which, as noted in Finding of Fact “1”, petitioner had acquired pay phones through a bulk sale. Mr. Ogrodnick described his duties as district manager as follows:

I run the office, the service technicians who I'm responsible for that go out and service and clean and collect the coins from the pay phones. There are installers of the pay phones that install and do heavy repairs on the pay phones. . . . We have coin counters. They count the coins from the pay phones. There is a secretary in the office, warehouse crew and parts and repair people, also (tr., p. 42).

Mr. Ogrodnick, who has been employed in the telecommunications industry for 11 years including 8 years in the pay phone industry, began as an installation repair technician employed by the New York Telephone Company. He was then employed as a pay phone installer and worked his way up to a position as service manager in charge of service technicians before then becoming a district manager.

9. Based upon his knowledge and experience, Mr. Ogrodnick considers himself to be an expert in the manner in which pay phones are installed and in the operation of the different components of pay phones. In his opinion, Mr. Ogrodnick testified that there are 21 essential or “necessary and integral parts of a pay telephone” (tr., p. 53) and described their particular functions as follows:

Essential part according to Mr. Ogrodnick	Mr. Ogrodnick’s description
1. Pedestal or wall mount	Houses the telephone company’s demarcation device ⁴ and secures and protects the pay phone and wires, including the power cable, that come through the pay phone and also keeps the pay phone at the proper height for use by customers in compliance with the Americans with Disabilities Act
2. Enclosure	Secures and protects the pay phone and keeps out the weather and may provide a sound barrier and house lighting
3. Upper housing	Outside shell that holds the keypad, handset, the coin release linkage and secures the computer board
4. Lower housing	Outside shell that holds the inner components
5. Computer board	Determines the rate of the pay phone and whether the call is placed
6. Coin mechanism	Accepts money and divides and separates out quarters, nickels and dimes
7. Trigger switch	Registers what the coin was with the computer board, a quarter, nickle or dime
8. Hopper	Holds the money until the call is placed or the money is returned to the user
9. Relay	Releases the money from the hopper in whatever direction is necessary
10. Coin chute	Where the user retrieves money if the call is not placed

⁴According to Mr. Ogrodnick, the pedestal is the “address” for purposes of the telephone company, i.e., Bell Atlantic, formerly NYXEX, to which “they go to ... install their wires and demarcation point” (tr., p. 94).

11. Anti-stuffing device (ASD)	Where money is collected from
12. Ribbon cable	Connects the computer board to the keypad in the upper housing unit
13. Power cord	Brings the power and dial tone from a Bell Atlantic (formerly NYNEX) wire to the computer board
14. Keypad	Number pad by which the call is placed
15. Handset	Black plastic cradle piece which holds the speaking and hearing (receiver) parts and wires
16. Coin release linkage	Linkage on the inside of the upper housing that catches and releases money to be returned to the user
17. Coin box	Holds money from completed calls
18. Vault door	Secures the coin box in the lower housing
19. Mast	Holds the wires coming into the pedestal
20. Coin release lever	Used by the customer to work the coin release linkage
21. Cradle	Holds the handset

10. Mr. Ogrodnick elaborated upon the functions of pedestals and enclosures as follows:

The main reason for the pedestals and enclosures are for protection and security. . . . [T]he lower housing gets mounted into the pedestal. The pedestal then gets mounted to the ground in some fashion and the enclosure gets mounted to the pedestal and the enclosure keeps out rain. It protects the upper housing and lower housing from vandalism. It's harder for anyone to get at the phone to vandalize it when the enclosure is around it (tr., pp. 61-62).

According to Mr. Ogrodnick, the pedestal, enclosure, telephone and mast are a “single integral unit” (tr., p. 68). Without a pedestal and enclosure, petitioner would not be able to operate a pay phone outdoors due to weather conditions and vandalism. In particular, Mr. Ogrodnick noted that the enclosure prevents the handset from being used by a vandal to break a glass window since it cannot be stretched around the enclosure.

11. Mr. Ogrodnick described the installation of pedestals and enclosures as follows:

The pedestal is attached to the ground in which we drill holes. We put bolts in the ground. We bolt down the pedestal to the ground and then we also weld those bolts so that the bolts won't be taken off and the whole pedestal removed. The enclosure is then bolted to the pedestal and the bolts are all hidden on the inside. Then when you put the lower housing in, it locks where you had attached the bolts to, so you can't get at the bolts, so it's all one unit at the end (tr., p. 87).

12. On cross-examination, Mr. Ogrodnick agreed that "signage" was not "necessary to initiate or receive calls" and pointed out that he did not include it on his list of 21 essential parts (tr., p. 107).

13. Although he did not know exact costs, Mr. Ogrodnick estimated that the standard pedestal, such as the Econoline, Number 23, cost "somewhere around \$200.00 and the enclosure about \$150.00" (tr., p. 110).

14. 85% of petitioner's installations of pay phones are outdoors, exposed to the elements.

15. Petitioner submitted 14 proposed findings of fact. Proposed findings of fact "1", "2", "3", "4", "5", "6", "7", "8", "9", "10", "11", "12", and "14" are accepted and incorporated into this determination. Proposed finding of fact "13" is an ultimate finding of fact, more in the nature of a conclusion of law, and will be addressed in the conclusions of law.

16. Petitioner has also proposed nine conclusions of law. However, there is no requirement in the law or regulations to rule on them (State Administrative Procedure Act § 307[1]).

SUMMARY OF THE PARTIES' POSITIONS

17. Petitioner contends that it "has demonstrated that the relationship between pedestals and enclosures, and the receiving or initiating of communication, is close, integral, dependent and necessary" (Petitioner's reply brief, p. 16). Further, according to petitioner, each and every function of the pedestals and enclosures is directly related to the capability of the pay phone to

receive or initiate communication so that they are used predominantly in receiving and initiating telephone communications. Petitioner points out that its pay phone receipts are subject to the imposition of sales tax and therefore the legislative policy of avoiding pyramiding of sales taxes “requires exemptions be granted to pedestals and enclosures” (Petitioner’s reply brief, p. 17).

Citing the decision of the Court of Appeals in *Matter of Burger King v. State Tax Commission* (51 NY2d 614, 623, 435 NYS2d 689, 693), petitioner maintains that the spirit underlying the sales tax law “is to impose the tax only upon the sale to the ultimate consumer, at which time the price paid for the taxable item would presumably be at its highest.” According to petitioner, the fact that pedestals and enclosures as components of a pay phone installation do not receive or initiate and switch communications is not determinative since they are part of an “integrated unit . . . eligible for exemption” (Petitioner’s brief, p. 13). Petitioner maintains that the Division should not be permitted “to microanalyze pay telephone installations on a component-by-component basis” (Petitioner’s brief, p. 26).

18. The Division counters that the exemption from sales tax for machinery and equipment used in production of tangible personal property is distinct from the exemption for telephone station apparatus used to receive, or initiate and switch telephone communication which “only exempts certain equipment used to perform a specific task” (Division’s brief, p. 22). Petitioner’s use of enclosures and pedestals is “in conjunction with telephone communication” and the enclosures and pedestals are not used to receive, switch or initiate telecommunications signals (Division’s brief, p. 3). Further, they are not used “directly” or “predominantly” to receive, switch or initiate telecommunication although the Division notes that “it may be true that the pedestals and enclosures provide support for the phone, protection from vandalism, [and] reduced exposure to weather” (Division’s brief, p. 25). According to the Division, petitioner has

merely shown that pedestals and enclosures support the operation of a pay phone business, which is insufficient for purposes of demonstrating entitlement to a sales tax exemption.

CONCLUSIONS OF LAW

A. Under Tax Law § 1105(a), sales tax is imposed upon “[t]he receipts from every retail sale of tangible personal property, except as otherwise provided in this article.” All sales of tangible personal property are presumptively subject to tax pursuant to Tax Law § 1132(c) “until the contrary is established.”

B. Tax Law § 1115(a) enumerates a lengthy list of various items of tangible personal property which are exempt from the imposition of sales tax on the receipts from the sale of such items. Included in this listing, at Tax Law § 1115(a)(12), as in effect during the years at issue,⁵ is the following:

Machinery or equipment for use or consumption directly and predominantly in the production of tangible personal property, gas, electricity, refrigeration or steam for sale, by manufacturing, processing, generating, assembling, refining, mining or extracting, *or telephone central office equipment or station apparatus or comparable telegraph equipment for use directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication*, but not including parts with a useful life of one year or less or tools or supplies used in connection with such machinery, equipment or apparatus. This exemption shall include all pipe, pipeline, drilling rigs, service rigs, vehicles and associated equipment used in the drilling, production and operation of oil, gas and solution mining activities to the point of sale to the first commercial purchaser. (Emphasis added.)

C. The Division is correct that exemptions from tax are strictly construed. “An exemption from taxation ‘must clearly appear, and the party claiming it must be able to point to some

⁵Laws of 1998 (ch 56, pt. A, § 94) inserted “or in receiving, amplifying, processing, transmitting and retransmitting telephone or telegraph signals” so that the exemption for telephone station apparatus now reads:

“or telephone central office equipment or station apparatus or comparable telegraph equipment for use directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication or in receiving, amplifying, processing, transmitting and retransmitting telephone or telegraph signals.”

provision of law plainly giving the exemption” (*Matter of Grace v. State Tax Commn.*, 37 NY2d 193,196, 371 NYS2d 715, 718, *lv denied* 37 NY2d 708, 375 NYS2d 1027 quoting *People ex rel. Savings Bank of New London v. Coleman*, 135 NY 231, 234). However, in addition, the statutory language providing the exemption must be construed in a practical fashion with deference to the legislative intent behind the exemption (*see, Matter of Qualex, Inc./Carhart Photo, Inc.*, Tax Appeals Tribunal, February 23, 1995).

D. The exemption for telephone station apparatus for use directly and predominantly in receiving or initiating and switching telephone communication was placed by the Legislature in the same section of the Tax Law as the exemption for production equipment commonly referred to as the manufacturing exemption. As a result, the exemption at issue has been viewed as a “parallel exemption” to the manufacturing exemption and may be claimed only by a purchaser of such equipment who is a vendor of telephone services for sale to customers, which are, in turn, subject to the imposition of sales tax (*Eastman Kodak Company v. Department of Taxation and Finance*, Sup Ct, Monroe County, November 22, 1989, Siracus, J.; *Matter of Cortelco*, Tax Appeals Tribunal, October 31, 1991; *see also, Matter of Stoddard Communications, Inc.*, Tax Appeals Tribunal, August 30, 1990). As noted in Finding of Fact “2”, petitioner had taxable sales from its operation of pay phones in New York, when annualized, of approximately \$10,000,000.00, so it is not barred from claiming the exemption like the taxpayers in the three matters cited. In addition, in construing the exemption at issue, prior matters involving the manufacturing exemption are relevant given the parallel nature of the manufacturing exemption.

E. The parties agree that pedestals and enclosures are telephone station apparatus, as required by the exemption at issue, pursuant to the Public Service Commission regulations at 16 NYCRR former 231. Consequently, at the crux of this matter is whether pedestals and

enclosures are telephone station apparatus for use “directly and predominantly” in receiving or initiating and switching telephone communications.

F. The terminology of “directly and predominantly” has been interpreted in the context of the manufacturing exemption. For example, in *Matter of Deco Builders* (Tax Appeals Tribunal, May 9, 1991), the Tribunal, in reversing the Administrative Law Judge, decided that the taxpayer’s purchase of certain custom-made wooden staves later assembled on site into a penstock was exempt from sales tax as the purchase of machinery or equipment used *directly* and *predominantly* in the production of tangible personal property for sale pursuant to the manufacturing exemption under Tax Law § 1115(a)(12). The Administrative Law Judge had determined that although the penstock was machinery and equipment within the meaning of the statutory provision at issue, it was used to produce electricity which was used in the production process, and therefore its relationship to production was secondary and did not have the “active causal relationship” to the product to be sold as required by the tax regulations at 20 NYCRR 528.13(c)(1). To the contrary, the Tribunal held that the penstock was directly used in production:

The determination as to whether a particular piece of machinery qualifies for the exemption depends upon the peculiarities of a taxpayer’s operation and must be individually assessed on its own fact pattern (*Matter of Rochester Independent Packer, Inc. v. Heckelman*, 83 Misc 2d 1064, 374 NYS2d 991, 993).

...[T]he penstock was a required element in the process of producing electricity at the Newton Falls paper mill. The electricity produced was used to run the machinery in the mill that made the paper. The Division argues that these facts show that the penstock’s relationship to production was secondary to production and insufficiently ‘active’ because it did not actually operate on the paper or on materials used to form the paper. We find this to be a strained interpretation of the language of the regulation. Clearly, electricity was an essential and active part of production at the mill, (in fact, there would have been no production process without electricity) [citations omitted].

Similarly, it may be concluded that without the pedestals there would have been no receiving or initiating of telephone communications at petitioner's pay phone installations. As noted in Finding of Fact "9", the function of the pedestals, as described by Mr. Ogrodnick's credible testimony, was essential to, and had an active causal relationship with, the operation of the pay phone. Without the pedestals, the computer board would function, if at all, for only a minimum period. Unsupported, unsecured, and unprotected, it is reasonable to conclude that it would fail or be damaged almost immediately without the support, security and protection provided by a pedestal. With regard to the enclosures, petitioner has met its burden that with reference to outdoor installations, the enclosures play a similar function to the pedestals: securing and protecting the computer board from damaging weather. However, with reference to indoor installations, the computer board could function without the installation of an enclosure to protect it from the elements.

G. Furthermore, the function (i) of the pedestals and (ii) of the enclosures when used in outdoor installations may also be viewed as *predominantly* related to the receiving or initiating of telephone communication. They do not serve any other *separate and distinct* use (*cf.*, ***Matter of Empire Vision Center, Inc.***, Tax Appeals Tribunal, November 7, 1991 [wherein the Tribunal noted that the computer at issue in that case performed another function besides production, i.e., administration]).

H. In addition, although the Division is correct that a taxpayer does not obtain an exemption from sales tax simply by complaining of possible "pyramiding of tax," granting the station apparatus exemption to pedestals and to enclosures, when used in outdoor installations, comports with the legislative intent in enacting the manufacturing and telephone station apparatus exemptions, i.e., to counteract the phenomenon of pyramiding sales tax (*see, American*

Communications Technology v. Tax Appeals Tribunal, 185 AD2d 79, 82, 592 NYS2d 147, 149, *affd* 83 NY2d 773, 611 NYS2d 125).

I. As noted in Finding of Fact “14”, 85% of petitioner’s installations of pay phones are outdoors, exposed to the elements. Consequently, 15% of petitioner’s installations of pay phones are indoors, and such percentage may be applied to the purchases at issue of approximately \$860,000.00 to determine a reasonable allocation to indoor installations. As noted in Finding of Fact “13,” Mr. Ogrodnick estimated that the standard pedestal costs approximately \$200.00 and an enclosure about \$150.00. Therefore, it is also reasonable to conclude that 42.86% of the amount allocated to indoor installations may be, in turn, allocated to the purchase of enclosures used in indoor installations. \$150.00 represents 42.86% of \$350.00, the total of Mr. Ogrodnick’s estimate for a pedestal of \$200.00 and an enclosure of \$150.00. Consequently, 42.86% of the portion of the purchases of pedestals and enclosures allocable to the indoor installations are subject to sales tax.

J. The petition of Peoples Telephone Company, Inc. is granted to the extent indicated in Conclusions of Law “F” and “I”, but, in all other respects is denied, and the Notice of Determination dated September 3, 1996 is to be modified to so conform.

DATED: Troy, New York
July 22, 1999

/s/ Frank W. Barrie
ADMINISTRATIVE LAW JUDGE